

BEFORE THE STATE BOARD OF EQUALIZATION
OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of
ROBERT M. AND JEAN W. BROWN

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Appearances :

For Appellants: Edward Sumner, Attorney at Law

For Respondent: Crawford H. Thomas, Associate Tax
Counsel

O P I N I O N

This appeal is made pursuant to section 18594 of the Revenue and Taxation Code from the action of the Franchise Tax Board on the protest of Robert M. and Jean W. Brown against a proposed assessment of additional personal income tax in the amount of \$391.11 for the year 1954.

Appellants filed their joint 1954 personal income tax return on the due date, April 15, 1955. The accountant who prepared the return inadvertently failed to report a sale by appellants of a partnership interest in 1954. Immediately upon discovering the omission, appellants on June 15, 1955, filed an amended return reporting the sale at a price of \$33,311.41 and the receipt in 1954 of \$5,274.21 toward the purchase price. In the amended return, the income from the sale was reported on the installment method under section 17532 (now 17578) of the Revenue and Taxation Code. The installment method permits a taxpayer to return as income in any year that proportion of the payments actually received in that year which the gross profit realized or to be realized when payment is completed, bears to the total contract price. (Rev. & Tax Code, Sec. 17531 (now 17577).)

Respondent acknowledges that the sale would qualify for treatment under the installment method had appellants made a timely election to use that method. It is contended, however, that the election could not be made after April 15, 1955, and that, therefore, the entire gain is taxable in the year of the sale.

Interpreting federal provisions substantially identical to those which concern us here, the Tax Court of the United States adopted and for a considerable period followed without deviation the principle that an election to use the installment method must be made in a timely return for the year of the sale. (Sarah Briarly, 29 B.T.A. 256; W. T. Thrift, Sr., 15 T.C. 366; Cedar Valley Distillery, Inc., 16 T.C. 870; John W. Commons, 20 T.C. 900; W. A. Ireland, 32 T.C. 994.) Following this line of decision, we adopted the same principle in Appeal of Estate of Worth G. Murdock, Cal. St. Bd. of Equal., June 22, 1956, 2 CCH Cal. Tax Cas. Par. 200-550, P-H State & Local Tax Serv. Cal. Bar. 58100.

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The rule, however, has been weakened in recent years by exceptions both in the Tax Court and other federal courts, exceptions announced in decisions which stressed the point that neither the statute nor the regulations specifically defined the time or manner of making the election. (John F. Bayley, 35 T.C. 288.; Jack Farber, 36 T.C. 1142, aff'd on other grounds, 312 F.2d 729, cert. denied, 374 U.S. 828 (10 L. Ed. 2d 1051); Nathan C. Spivey, 40 T.C. 1051; Hornberger v. Commissioner, 289 F.2d 602; Nunn v. Gray, 196 F. Supp. 305.)

Among the cited cases in which exceptions were made, the Hornberger decision bears a close resemblance to appellants' situation. That case involved a sale in which part of the purchase price was received in cash at the time of the transaction. The taxpayers employed a firm of accountants to prepare their returns and directed them to treat the gain on the sale under the installment method. Due to an error by the accounting firm, the sale was not reported at all in the returns which were filed for that year. Holding that the taxpayers could nevertheless use the installment method, the court stated that:

If a failure to report an income producing sale is excusable and may be corrected without penalty for all other purposes of the income tax laws, we perceive no reason why, if reported or claimed as an installment sale while the year of sale is still open to adjustment under the statute and if it has not been treated in an inconsistent manner, this should not entitle the taxpayer to installment treatment of the sale.

Although the facts surrounding the omission of a report of the sale in appellants' original, timely return have not been specified in full detail, respondent does not contend that appellants were negligent and it is our impression that they were not. Like the circumstances in Hornberger, the omission here was due to an oversight by the accountant who prepared the return. The fact that appellants filed an amended return correcting the inadvertent omission within two months after the original return was timely filed demonstrates that there was an honest error and that appellants acted in good faith. So far as we can ascertain, appellants neither sought nor obtained any advantage by the omission.

Upon the particular facts of this case, we conclude that appellants are entitled to use the installment method of reporting their gain from the sale in question.

O R D E R

Pursuant to the views expressed in the opinion of the board on file in this proceeding, and good cause appearing therefor,

IT IS HEREBY ORDERED, ADJUDGED AND DECREED, pursuant to section 18595 of the Revenue and Taxation Code that the action of the Franchise Tax Board on the protest of Robert M. and Jean W. Brown against a proposed assessment of additional personal income tax in the amount of \$391.11 for the year 1954, be and the same is hereby reversed.

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Done at Sacramento, California, this 10th day of December, 1963,
by the State Board of Equalization,

_____John W. Lynch_____, Chairman

_____George R. Reilly_____, Member

_____Paul R. Leake_____, Member

_____Richard Nevins_____, Member

_____, Member

ATTEST: _____H.F. Freeman_____, Secretary